

2007 U.S.-China Commission Trip to China and Hong Kong

Trip Summary

From April 22 to May 1, members of the U.S.-China Economic and Security Commission traveled to Beijing, Dalian, Anshan, Shenyang, and Hong Kong for the purpose of observing and assessing the economic and security implications of the U.S. relationship with China. The delegation met with Chinese government officials, Hong Kong government officials, representatives from the People's Liberation Army (PLA), American, Chinese, and Hong Kong businesspeople, and U.S. diplomats. Throughout the course of this visit, the delegation examined issues related to Chinese military modernization and strategy; U.S. investment in China and transfer of production activities from the United States to China; China's compliance with World Trade Organization (WTO) agreements; China's energy policies and energy-related activities; freedom of expression in China; and China's political and commercial relationship with Hong Kong.

In Beijing, Jin Xu, Deputy Director General of the Department of American and Oceanic Affairs at the Ministry of Commerce, acknowledged the existence of intellectual property (IP) violations in contrast to his statement last year that China had no IP protection problem. During this year's meeting, he argued that IP protection is a concern of China. China has established an Intellectual Property Rights Working Group to address the regulation and enforcement of intellectual property across government ministries. This group's 2007 plan lists over 270 measures to address this problem from multiple perspectives, including legislation, law enforcement, institution building, publicity, training and education. In addition, the government has linked its goal of promoting indigenous scientific innovation to the protection of intellectual property rights. Despite these efforts, other representatives from the Ministry stated that as the volume of trade between the United States and China continues to grow, they do not expect the IPR problem between our two countries to become smaller.

When discussing the issue of economic subsidies and the recent filing by the United States of a WTO case against China for industrial subsidies, the Ministry of Commerce indicated that the focus of China's industrial development is changing to energy and infrastructure, including transportation. For example, the aviation industry is nascent, and the Chinese government will enact concrete measures to support its development. A legal representative from the Ministry of Commerce stated that WTO agreements allow members to provide subsidies to certain sectors. He argued that the United States has miscalculated the extent and magnitude of subsidies; the impression that China is unfairly subsidizing its industries is the erroneous idea of the U.S. Commerce Department caused by its use of surrogate benchmarks to calculate the subsidy margin and by double counting.

At the Ministry of Foreign Affairs, Xie Feng, Deputy Director General for North American Affairs, highlighted several issues of importance to the U.S.-China relationship, including economic relations, the commitments of the Bush Administration to the one-China policy, coordination on regional and global issues, and China's political reform. He acknowledged that in each area there are avenues of cooperation and sources of tension. For example, China perceives that those in Taiwan who support complete independence are in the minority and do not act in the interest of the majority who support reunification or maintaining the status quo. The PRC government remains concerned about U.S. arms sales to Taiwan. Xie requested that the United States encourage Taiwan's authorities to provide more access to Taiwan for Chinese journalists.

When Commissioners asked Xie about China's January 2007 anti-satellite (ASAT) test, he stated that China did not conduct the test for the purpose of changing its policies on outer space or air space. China subscribes to the classical definition of sovereignty, and Xie argued that the nations of the international community should cooperate to ensure transit rights through air and space for commercial purposes. He said that the government considered the ASAT test a "normal scientific test," and realized only after the very negative international response that further explanation was needed. Xie confirmed that the test was approved by the Chinese leadership, including President Hu. With regard to arms control policy in China, Xue told the Commissioners that, primary responsibility in the Chinese government for implementing arms control treaties does not reside in one ministry; but is conducted in coordination by the Ministries of Foreign Affairs and Defense.

Xue cited the effort to resolve the North Korean nuclear situation as an important example of U.S.-China coordination on regional and global issues. He stated that the initial action plan announced on February 13 is an important stage toward the final denuclearization of the North Korean peninsula. Despite the fact that the first deadline for North Korean action to implement the action plan had passed when Commissioners were meeting with him, Xue resisted labeling North Korea as noncompliant with the agreement because it refused to shut down the Yongbyon nuclear reactor until its impounded funds at Banco Delta Asia in Macau are released.

With respect to other foreign relations matters, Xie said that China is encouraging positive change in Sudan to resolve the conflict in Darfur, which he said was encouraged by President Hu when he visited Khartoum during his tour of Africa in February. Deputy Foreign Minister Zhai Jun recently visited the Darfur region at the request of the Sudanese government, and he reported that his impression does not match what the media are describing, especially in the refugee camps. Xie argued that resolution of the Darfur conflict must be pursued on dual tracks: first, by pressuring the Sudanese government to accept United Nations peacekeeping forces, and second, by bringing the opposition forces into the political process.

Representatives from the China Institute of International Studies (CIIS) also stated that China seeks a positive role in the Middle East peace process and in promoting a peaceful resolution to the Iranian nuclear issue. China believes that the peace process should be based on two principles: first, the United Nations resolution, and second, the

land-for-peace principle. China also supports the European Union's efforts to consult with Iran and peacefully resolve international concerns about Iran's ambitions to develop nuclear weapons. Gong Xianfu, President of CIIS, also stated that as a responsible country, China has abided by its international commitments to control the sale and transfer of missiles and missile technology and has not provided any related assistance to Iran since making those commitments.

The delegation met with People's Liberation Army (PLA) scholars and strategists at the PLA Academy of Military Sciences. This meeting was the first formal meeting between the U.S.-China Commission and representatives of the PLA, as in previous years Commission requests for such meetings had been denied by the Chinese government. During this discussion, the officers stated that the trend of Chinese military transformation will continue toward informationalization with a focus on modernizing air, naval, and strategic missile forces. The primary goal for the Army's modernization is to increase maneuverability; the primary goal for the Air Force is to increase offensive strike capabilities; and the primary goal for the Navy is to shift offshore and develop a blue water capability. The goal for the Second Artillery is to "rebalance" nuclear and conventional missile forces. In addition to developing and refining its ability to conduct informationalized warfare, the PLA recognizes that it must have integrated information networks, which necessitates an active presence in space.

One of the PLA's missions is to protect China's development interests. The officers noted that they would defend Chinese interests in the region and around the world, especially important sources of energy for China. This requires a force projection capacity that, in turn, supports developing a blue water navy. They argued that U.S. concerns are misplaced about China's military modernization and its lack of transparency. In their opinion, the lack of understanding of China's intent is not due to China's failure to reveal its intent but to a lack of trust or confidence on the part of the United States.

PLA officers analyzed the U.S.'s concept of global strike from two viewpoints: strategic and operational. Strategically, they argued that the concept is destabilizing because it threatens rather than strengthens the stability of the nuclear threshold. If a country fears the United States might strike it, it may react preemptively, which would be further destabilizing. However, from an operational standpoint, the global strike concept raises the threshold of nuclear warfare because it offers more operational/tactical (conventional) options. Therefore, in the PLA's analysis, global strike is strategically destabilizing but concurrently contributes to tactical stability by reducing the probability of nuclear escalation.

When questioned about cyber attacks, officers at the Academy noted that scholars hold differing opinions about whether a computer network attack may constitute an act of warfare. Some believe it meets that definition, but others believe that a network attack alone without corresponding conventional attacks is not an act of warfare. Officers said that if a cyber attack targets military capabilities of another country and does significant damage, conventional counterattacks are warranted. However, they noted the difficulty in

accurately identifying the source of cyber attacks and argued that the source must be clearly identified before a counterattack is launched.

In Liaoning province in northeastern China, the delegation visited the cities of Dalian, Anshan, and Shenyang. Throughout this visit, the province showcased its economic development that relies upon the development of Dalian as an export base for the region that in turn supports the development of inland manufacturing. The northeast region of China has maintained economic growth rates higher than the national average in recent years and is poised to continue this explosive growth through the integration of value-added manufacturing, high-technology production, and intraregional shipping.

The Dalian Commodity Exchange (DCE) was established in 1993, and now is one of three commodity markets authorized by the central government. This exchange trades corn, soy, soymeal, and soy oil, and last year was the ninth largest exchange in the world. The DCE has a memorandum of understanding with the Chicago Mercantile Exchange that includes information sharing and employee training. Cargill is a member of this commodity exchange, along with French and Japanese companies.

The Dalian Free Trade Zone oversees the bonded port area, which will officially enter operation by the end of this year. The central government identified three container terminals under development and adjacent land that will be used as a bonded port area outside of the administration of Chinese customs officials. Once domestic cargo enters the fence surrounding the area, it automatically will be considered exported, and domestic producers can claim a tax rebate. Within the bonded port area, goods may be imported, further processed, and then re-exported.

Businesses in this area are integrating their strategic development to take advantage of Dalian's port location and trade promotion policies. For example, the delegation visited Brilliance Auto Company in Shenyang, which manufactures high-end sedans for export to Europe. The sedans are then transported to the Dalian Auto Terminal where they are loaded onto ships; the terminal has a capacity of 750,000 automobiles per year. Additionally, Dalian has developed an industrial park to export software and provide information services for high technology companies. Forty-three percent of the companies located in this park are foreign companies, including IBM, Hewlett Packard, GE, Sony, Accenture, and Panasonic.

The delegation visited two U.S. companies with production facilities in Liaoning province: Goodyear Tire in Dalian and GE in Shenyang. Goodyear Dalian started production in 1995 and is the largest Goodyear plant in Asia. Most of its tires are produced for the Chinese market. (The Ministry of Agriculture maintains a 20 percent duty on imported natural rubber that limits the ability of Chinese-manufactured rubber products to compete internationally.) However, this pricing policy also affects Chinese domestic tire producers. Goodyear signed a 52-year lease with the local government on the land where its Dalian plant is located, but recently has seen the government encourage residential development around the periphery of the plant that limits its ability to expand.

GE has three ventures in Shenyang that manufacture turbine components, assemble wind turbines, and service gas turbines. According to GE representatives, demand for wind turbines is increasing in China as the government seeks to diversify its energy resources. GE faces competition from local manufacturers primarily because the local firms are able to source their components domestically. The more components that GE must import, the more expensive the assembly of turbines becomes. GE representatives argued that international companies are being forced to localize their parts supplies in order to remain competitive in the Chinese market.

The delegation toured the facilities of two traditional state-owned enterprises in the northeast: an iron and steel factory and an oil refinery. The Anshan Iron and Steel Company was constructed by the Japanese during the period of Manchurian occupation and has played a key role in China's heavy industry since that time. Today it is the second largest steel producer in China and produces items such as pipes, rails, containers, and automobile frames. The PetroChina Fushun Petrochemical Company Refinery No. 1 is one of the oldest refineries in China. The refinery's site the delegation visited primarily produces paraffin wax for foodstuffs and packaging. Nearly half this paraffin wax is exported. Others of the refinery's sites process lubricating oils. These state-owned companies are redefining their image as industrial leaders in northeast China by reducing the social function each plays and by supporting the development of regional manufacturing and infrastructure.

In Hong Kong, the delegation met with American businesspeople, Hong Kong government officials, Hong Kong democratic activists and environmentalists, and the U.S. Consul General and his staff. In general, Hong Kong's economy and political system have recovered from the turmoil of the Asian financial crisis, Severe Acute Respiratory Syndrome (SARS) epidemic, and protests over insufficiently rapid progress toward democratization since China regained political control of Hong Kong in 1997. Polls indicate that Hong Kong's people increasingly identify themselves as Chinese, and Hong Kong has increased its instruction of Mandarin Chinese in schools. American business representatives noted that Chinese companies often seek to locate branches in Hong Kong to take advantage of the jurisdiction's judicial system, law enforcement, and services infrastructure. For example, Hong Kong's protection and enforcement of intellectual property rights are superior to mainland China's, and Chinese businesses tend to keep their higher value-added materials in Hong Kong to better protect them.

The environment is one of the most popular political issues in Hong Kong, as Hong Kong residents struggle to deal with locally-produced air and water pollution and also with pollution generated in mainland China. In China, enforcement of environmental regulations at the local level remains a major problem, and this has a negative public health impact on the people in those communities and those who live with the downstream effects of the pollution. Guangdong Province, adjacent to Hong Kong, is the first province in China to release air quality data, and Hong Kong has established some cooperative efforts with Guangdong to address air and water quality problems. Another air quality problem unique to this area, identified by Christine Loh of Hong Kong's Civic Exchange, is the pollution created by ships utilizing the container ports. These ships' emissions remain

localized at ground level. Ng Chonam of the University of Hong Kong also noted that water has become a major issue in all cities in China, including Guangzhou and Hong Kong. During the dry season in Guangzhou, the outflow of the Pearl River diminishes to the point that sea water surges into the delta, thus harming the water supply and surrounding environment. Hong Kong now imports water from Guangdong province, so this is of concern to Hong Kong as well.

During the campaign of candidates running in the March 2007 election for Hong Kong's Chief Executive, incumbent Chief Executive Donald Tsang agreed to participate in two debates with Alan Leong, the candidate who represented pro-democratic parties in Hong Kong. These debates were watched by over two million people in Hong Kong and, notably, the Chinese government permitted the broadcasts to be viewed in Guangdong Province. Although Leong did not win the election, the support he garnered helped to establish a significant precedent and the expectation that future elections for Chief Executive will have multiple candidates and proposed policy platforms as well as open debates.

Reelected Chief Executive Tsang's leadership is perceived by the public to be improving although his government continues to stall movement toward universal suffrage, which many political observers believe will not be approved until 2017 at the earliest, a full twenty years after the governance of Hong Kong was returned to China. Tsang has pledged to resolve the issue of universal suffrage before the end of his term in 2012, and is expected to produce a green paper on constitutional development this summer that will present several options for universal suffrage. After a period of public consultation, Hong Kong officials have indicated they will adopt the option with the broadest support (determined by public polls) and present that option to the Chinese government for approval. Democratic activists expressed concern that the pro-Beijing forces in Hong Kong will try to manipulate the polls through their presentation of the options. If they succeed, pro-democratic forces would be placed in the difficult position of either accepting an option that offers less than complete or direct universal suffrage as is guaranteed in the Basic Law, or appearing obstructionist to political reforms favored by a majority of Hong Kong's citizens.